



Contract Management

Briefing for Acquisition Advisory Panel on
Commercial Practices/Commercial Items,
Contracts for Services and Interagency
Contracting, and Performance Based
Contracts for Logistics Support

May 17, 2005

Commercial Practices/Commercial Items

Background

- The Federal Acquisition Streamlining Act of 1994 (FASA) and the Federal Acquisition Reform Act of 1996 (FARA) were designed to **streamline acquisition laws, facilitate the acquisition of commercial products, and eliminate unnecessary statutory impediments to efficient and expeditious acquisition**. One impact of the Acts was to **significantly broaden the commercial item definition and allow more sole-source items to qualify for the “commercial item” exception to cost or pricing data**.
- The Truth in Negotiations Act of 1962 (TINA) allows DoD to obtain cost or pricing data (certified cost information) from Defense contractors to **ensure the integrity of DoD spending** for military goods and services that are not subject to marketplace pricing.
- In June 1995, the Director, Defense Procurement provided comments on the benefits of TINA, marketplace pricing, and the differences between DoD and commercial procurement environments.

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Background (continued)

- “The requirements of TINA are necessary to ensure the integrity of DoD spending for military goods and services that are not subject to marketplace pricing. **When there is a market that establishes prices by the forces of supply and demand, the market provides the oversight.** DoD procures many highly complex military systems in the absence of supply/demand situations for these relatively low volume, unique military goods. The requirements of TINA address legitimate and necessary differences between DoD and commercial procurement environments.”
- “While DoD recognizes the need for TINA, it also is moving to increase competition and decrease the number of pricing actions that would require cost or pricing data. The implementation of FASA, with its emphasis on encouraging the acquisition of commercial end items and increased competition, will bring the requisite market forces to bear on prices, and thus exempt contractors from the requirement to submit cost or pricing data. **Absent this competition, the quantitative benefit to the Government of TINA compliance far exceeds the cost of Government oversight.**”

Commercial Practices/Commercial Items

Guidance

FAR 2.101 -- Definitions. "Commercial item" means --

(1) Any item, other than real property, that is **of a type** customarily used by the general public or by non-governmental entities for purposes other than governmental purposes, and--

- (i) **Has been sold**, leased, or licensed to the general public; or,
- (ii) **Has been offered for sale**, lease, or license to the general public;

(2) **Any item that evolved from an item** described in paragraph (1) of this definition through advances in technology or performance and that is not yet available in the commercial marketplace, but will be available in the commercial marketplace in time to satisfy the delivery requirements under a Government solicitation;

(3) Any item that would satisfy a criterion expressed in paragraphs (1) or (2) of this definition, but for --

- (i) **Modifications of a type customarily available** in the commercial marketplace; or
- (ii) **Minor modifications of a type not customarily available** in the commercial marketplace made to meet Federal Government requirements. Minor modifications means modifications that do not significantly alter the nongovernmental function or essential physical characteristics of an item or component, or change the purpose of a process. Factors to be considered in determining whether a modification is minor include the value and size of the modification and the comparative value and size of the final product. Dollar values and percentages may be used as guideposts, but are not conclusive evidence that a modification is minor;

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Guidance (continued)

- (5) Installation services, maintenance services, repair services, training services, and **other services** if--
 - (i) **Such services are procured for support of an item referred to in paragraph (1), (2), (3), or (4) of this definition**, regardless of whether such services are provided by the same source or at the same time as the item; and
 - (ii) The source of such services provides similar services contemporaneously to the general public under terms and conditions similar to those offered to the Federal Government;
- (6) **Services of a type offered and sold competitively in substantial quantities** in the commercial marketplace based on established catalog or market prices for specific tasks performed or specific outcomes to be achieved and under standard commercial terms and conditions. This does not include services that are sold based on hourly rates without an established catalog or market price for a specific service performed or a specific outcome to be achieved. For purposes of these services—
 - (i) “Catalog price” means a price included in a catalog, price list, schedule, or other form that is regularly maintained by the manufacturer or vendor, is either published or otherwise available for inspection by customers, and states prices at which sales are currently, or were last, made to a significant number of buyers constituting the general public; and
 - (ii) “Market prices” means current prices that are established in the course of ordinary trade between buyers and sellers free to bargain and that can be substantiated through competition or from sources independent of the offerors.

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Guidance (continued)

FAR 15.402 -- Pricing Policy. Contracting officers must –

(a) Purchase supplies and services from responsible sources **at fair and reasonable prices**. In establishing the reasonableness of the offered prices, the contracting officer **must not obtain more information than is necessary**. To the extent that **cost or pricing data are not required** by 15.403-4, the contracting officer must generally use the following **order of preference** in determining the type of information required:

(1) No additional information from the offeror, if the price is based on adequate price competition, except as provided by 15.403-3(b).

(2) Information other than cost or pricing data:

(i) Information related to prices (e.g., established **catalog** or market prices or **previous contract prices [price analysis]**), relying **first** on information available within the **Government**; **second**, on information obtained from **sources other than the offeror**; and, **if necessary**, on information obtained from the **offeror**. When obtaining information from the offeror is necessary, unless an exception under 15.403-1(b) (1) or (2) applies, such information submitted by the offeror shall include, at a minimum, appropriate **information on the prices at which the same or similar items have been sold previously, adequate for evaluating the reasonableness of the price**.

(ii) Cost information, that does not meet the definition of cost or pricing data at 2.101.

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Guidance (continued)

FAR 15.402 -- Pricing Policy. (continued)

3) *Cost or pricing data.* The contracting officer should use every means available to ascertain whether a fair and reasonable price can be determined **before requesting cost or pricing data.** Contracting officers **must not require unnecessarily the submission of cost or pricing data, because it leads to increased proposal preparation costs, generally extends acquisition lead time, and consumes additional contractor and Government resources.**

FAR15.403 -- Obtaining Cost or Pricing Data.

15.403-1 -- Prohibition on Obtaining Cost or Pricing Data (10 U.S.C. 2306a and 41 U.S.C. 254b).

(a) Cost or pricing data shall not be obtained for acquisitions at or below the simplified acquisition threshold.

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Guidance (continued)

15.403-1 -- Prohibition on Obtaining Cost or Pricing Data (10 U.S.C. 2306a and 41 U.S.C. 254b). (continued)

(b) *Exceptions to cost or pricing data requirements.* The contracting officer shall not require submission of cost or pricing data to support any action (contracts, subcontracts, or modifications) (but may require information other than cost or pricing data to support a determination of price reasonableness or cost realism) --

(1) When the contracting officer determines that prices agreed upon are based on adequate price competition (see standards in paragraph (c)(1) of this subsection);

(2) When the contracting officer determines that prices agreed upon are based on prices set by law or regulation (see standards in paragraph (c)(2) of this subsection);

(3) *When a commercial item is being acquired* (see standards in paragraph (c)(3) of this subsection);

(4) When a waiver has been granted (see standards in paragraph (c)(4) of this subsection); or

(5) When modifying a contract or subcontract for commercial items (see standards in paragraph (c)(3) of this subsection).

Commercial Practices/Commercial Items

Guidance (continued)

Director, Defense Procurement Guidance. On August 2, 2000, the Director, Defense Procurement issued a memorandum to the Defense community on “**Obtaining Information for Pricing Sole-Source Commercial Items.**” The Director Stated:

“Please **remind you contracting professionals** that the clause at FAR 52.215-20 should be **included in the solicitations for sole-source commercial items** when the contracting officer has a reasonable expectation that **the offeror will request a commercial item exception to a requirement for submission of certified cost or pricing data**, and that the offeror will need to provide, at a minimum, appropriate information on the prices at which the same or similar items have been previously sold.”

FAR 52.215-20 states:

“ (ii) *Commercial item exception.* For a commercial item exception, the offeror shall submit, at a minimum, information on prices at which the same item or similar items have previously been sold in the commercial market that is adequate for evaluating the reasonableness of the price for this acquisition.”

(A) For catalog items, . . . Also explain the basis of each offered price and its relationship to the established catalog price, including how the proposed price relates to the price of recent sales in **quantities similar to the proposed quantities.**

Commercial Practices/Commercial Items

Commercial Item Determinations

- “All of these items fall into groups of equipment that are “of a type” (shares common traits or characteristics that distinguish the end items/parts as an identifiable group or class; and has the features of the group or class), and “sold” to the “general public.” The items are manufactured, assembled, and tested by the same workforce, in the same facilities with the same equipment, and under the same quality system as our commercial products.”
- “As you know, FAR Part 12, Acquisition of Commercial Items, was designed to provide the Department of Defense with greater access to commercial items with a preference for simplified price analysis as a means of determining price reasonableness. Additionally, the FAR re-write revised the definition of commercial items to include “similar or of a type” items, thus expanding the commercial market.”
- “He stated it is not politically popular at this juncture to restrict commercial determinations.”

Commercial Practices/Commercial Items

Contracting Officer and Contractor Statements

- “. . . NSNs that are determined to be sole source to [the contractor] meet the definition of commercial item per FAR 2.101(3)(ii), based on the **items are being manufactured on an integrated production line**, with little differentiation between the commercial and government items.”
- “I have determined that the items described above are commercial within the broad definition set forth in FAR 2.101. Still, I do not believe that this definition as written captures the **intent or spirit that was intended by Congress when this legislation was developed**. Congress’ intent was to allow the Government the advantages of the commercial marketplace in procuring supplies and services. I do not believe its intent was to create such **broad sweeping categories that everything purchased in the aerospace industry could be determined commercial**, but provide none of the advantages of the commercial marketplace.”

Commercial Practices/Commercial Items

Audit Coverage

- Commercial and Noncommercial Sole-Source Items Procured on Contract N000383-93-G-M111, Report No. 98-064, February 6, 1998
- Sole-Source Prices for Commercial Catalog and Noncommercial Spare Parts, Report No. 98-088, March 11, 1998
- Commercial Spare Parts Purchased on a Corporate Contract, Report No. 99-026, October 30, 1998
- Sole-Source Commercial Spare Parts Procured on a Requirements Type Contract, Report No. 99-217, August 16, 1999
- Sole-Source Noncommercial Spare Parts Orders on a Basic Ordering Agreement, Report No. 99-218, July 27, 1999
- Procurement of the Blade Heaters for the C-130 and P-3 Aircraft, Report No. D-2000-099, March 8, 2000
- Sole-Source Spare Parts Procured From an Exclusive Distributor, D-2004-012, October 16, 2003
- Acquisition of the Boeing KC-767A Tanker Aircraft, D-2004-064, March 29, 2004
- Audit of Spare Parts Procurements from AeroControlex Group, Project No. D2004-CH-0189, Ongoing
- Audit of the Air Force Strategic Supplier Initiative with Hamilton Sundstrand Corporation, Project No. D2005-CH-0183, Ongoing

Commercial Practices/Commercial Items

Audit Issues

- DoD paid modestly **discounted catalog prices** for **sole-source commercial items** that were **significantly higher than previous cost-based prices**.
- DoD paid **significantly higher prices for commercial** and noncommercial spare parts purchased on a sole-source basis, **than previous competitive purchases** of the same items.
- DoD paid **higher prices for commercial items** and **failed to take advantage of commercial practices such as direct vendor delivery** that would help offset the higher commercial prices.
- DoD, **using price analysis**, paid prices that were **higher than fair and reasonable as determined by cost analysis**.
- **No commercial market exists** in order to establish reasonable prices by the forces of supply and demand and the **commercial item procurement strategy did not provide sufficient cost or pricing data to conclude that prices negotiated represent a fair expenditure** of DoD funds.
- DoD, **using cost analysis**, **obtained fair and reasonable prices** for sole-source commercial items, and also improved delivery times and reduced Government inventory.

Commercial Practices/Commercial Items

DLA/Honeywell Strategic Supplier Alliance (to resolve audit issues)

- Used a Rapid Improvement Team Process (Facilitator, DoD, DLA, IG, DCAA, Honeywell).
- Tailored Support (Contractor or DLA inventory items based on demand and economic order quantities, profit based on level of support)
- Long-term FAR Part 15 contract (CAS Waiver)
- **No commercial item determinations**
- One Pass **Cost-Based** Pricing (DLA, DCAA, and IG review cost data with Honeywell pricer to determine fair and reasonable prices, economic order quantities, and support method)
- Results were lower prices, reduced number of negotiated orders, reduced administrative lead-time, and reduced Government inventory.
- Pricing problems easily resolved

Commercial Practices/Commercial Items

Consumer Report Recommends

To get a good price when buying a new car:

- Learn the Lowest Cost
- Always bargain up from the cost, never down from the sticker price

Contracts for Services and Interagency Contracting

Audit Coverage

- Contracts for Professional, Administrative, and Management Support Services, Report No. D-2000-100, March 10, 2000
- Multiple Award Contracts for Services, Report No. D-2001-189, September 30, 2001
- Contract Actions Awarded to Small Businesses, Report No. D-2003-029, November 25, 2002
- Contracts for Professional, Administrative, and Management Support Services, Report No. D-2004-015, October 30, 2003
- Contracts Awarded for the Coalition Provisional Authority by the Defense Contracting Command – Washington, Report No. D-2004-057, March 8, 2004
- DoD Purchases Made Through the General Services Administration (Draft Report)

Contracts for Services and Interagency Contracting

Audit Issues

- Lack of Good Market Research
 - Contracts and Task Orders awarded on a sole-source basis. (Exceptions claimed without support)
 - Program and Contracting offices have “desired” contractors.
- Scope of Work not Definitive
 - Requirements written are very broad and in general terms.
 - Conversely, some contracts clearly disclosed personnel services contracts.
 - Missing periods of performance.
- Numerous Funding Problems when MIPR's are Used
 - Used expired appropriations to award contracts.
 - No bona fide need in the Fiscal Year.
 - Used funds of wrong appropriation.
 - Not tracking and monitoring funds.

Contracts for Services and Interagency Contracting

Audit Issues (continued)

- Use of Multiple-Award Contracts Needs Improvement
 - Fair opportunity not given to all awardees.
 - Use of down-select procedures.
 - Work was awarded that was not suitable or within scope for a multiple award contract.
 - Use of sub-Task Orders
- Misuse of Federal Supply Schedules
 - Out of scope purchases.
 - No determination that a fair and reasonable price is being paid.
- Use of Cost-Reimbursable Contracts for Follow-up Requirements
 - Lack of FFP performance-based contracts on repetitive purchases.
 - Overuse of T&M contracts.

Contracts for Services and Interagency Contracting

Audit Issues (continued)

- Fair and Reasonable Prices not Assured
 - Reviews of labor hours, labor mixes, and rates not being performed.
 - Discounts for large Federal Supply Schedule buys not obtained.
 - Poor reviews of contractor price lists to determine fair prices.
 - No support for prices paid.
- Little Surveillance on Service Contracts
 - Invoices paid without review.
 - Purchasing level of effort, so it is difficult to determine whether we get what we paid for.
 - Lack of surveillance plans.
 - COR's not always appointed or lack knowledge of their roles.
 - Lack of reporting contractor performance.

Performance-Based Contracting for Logistics Support

Performance-Based Logistics (PBL)

- PBL first proposed by the Aerospace Industries Association as a preferred sustainment strategy in 1999.
- DoD endorsed the strategy as part of Future Logistics Enterprise and Quadrennial Defense Review.
- Deputy Secretary of Defense requires each Service to aggressively implement PBL.

Performance-Based Contracting for Logistics Support

PBL Questions

- Can PBL contracts improve performance and also reduce costs?
- Does industry have innovative and creative solutions to improve performance and reduce costs?
- Is DoD willing to pay more for improved performance on PBL contracts?
- How does DoD evaluate performance, both technical and cost?

Performance-Based Contracting for Logistics Support

Audit Coverage

- Commercial Contract for Total Logistics Support of the Aircraft Auxiliary Power Units, Report No. D-2000-180, August 31, 2000
- Industrial Prime Vendor Program at the Air Force Air Logistics Centers, Report No. D-2002-112, June 20, 2002
- F/A-18E/F Integrated Readiness Support Teaming Program, Report No. D-2003-120, August 8, 2003

Performance-Based Contracting for Logistics Support

Audit Issues

- The information used in the business case analysis was questionable and overstated the cost of DoD performance and likely benefits.
- The impact of transferring management responsibility for procurement and management of consumable items for selective “prime” customers from DLA was not considered
- The program improved availability but was using 55 additional personnel to manage material and failed to use \$9 million of available material in Defense Depots.
- The program did not consider issues relating to supply infrastructure, contracting methods, and inventory investment.

Performance-Based Contracting for Logistics Support

Audit Issues (continued)

- The cost-plus contract did not effectively implement the performance based material management and reliability improvement described in the acquisition plan. The contract failed to:
 - Reduce repair cycle times.
 - Achieve a minimum 10 percent reliability improvement from baseline calculations.
 - Reduce and effectively monitor infrastructure support costs to include Navy inventory investment.
 - Procure items directly from OEMs to reduce pass-through cost.
 - Accurately charge fleet customers.

FY 2004 DD 350 Contract Actions Over \$25K (\$billions)

	<u>Competitive</u>		<u>Non-Competitive</u>		<u>Totals</u>		<u>Performance Based</u>	
<u>RDT&E</u>	<u>Actions</u>	<u>Dollars</u>	<u>Actions</u>	<u>Dollars</u>	<u>Actions</u>	<u>Dollars</u>	<u>Actions</u>	<u>Dollars</u>
Fixed Price	5,896	1.44	1,820	1.55	7,716	2.99	1,150	0.33
Cost	19,202	20.22	4,670	8.49	23,872	28.71	5,244	6.59
Time & Materials	3,439	0.68	813	0.12	4,252	0.8	2,322	0.34
Labor Hours	153	0.05	57	0.01	210	0.06	32	0.01
Not Specified	0	0	0	0	0	0	1	0
Totals	28,690	22.39	7,360	10.17	36,050	32.56	8,749	7.27
 <u>Other Services</u>								
Fixed Price	181,896	41.99	66,055	9.96	247,951	51.95	43,184	14.86
Cost	35,267	22.96	6,752	6.22	42,019	29.18	14,414	14.32
Time & Materials	11,111	5.32	3,966	1.47	15,077	6.79	4,944	2.29
Labor Hours	2,467	0.37	951	0.19	3,418	0.56	418	0.07
Not Specified	23,688	6.15	0	0	23,688	6.15	5,000	1.99
Totals	254,429	76.79	77,724	17.84	332,153	94.63	67,960	33.53
Total Services	283,119	99.18	85,084	28.01	368,203	127.19	76,709	40.80
Commercial Services¹	83,968	14.35	29,561	3.03	113,529	17.38		
 <u>Supply</u>								
Fixed Price	176,263	40.67	77,730	41.66	253,993	82.33	0	0
Cost	1,494	3.24	3,222	10.91	4,716	14.15	0	0
Time & Materials	354	0.18	638	0.33	992	0.51	0	0
Labor Hours	52	0.02	48	0.20	100	0.22	0	0
Not Specified	63,152	4.69	0	0	63,152	4.69	0	0
Totals	241,315	48.80	81,638	53.10	322,953	101.90	0	0

¹Commercial Services are included in RDT&E and Other Services Totals